

**St. Lawrence Seaway Pilots' Association  
Contract # GS-23F-0124M**

**Independent Accountant's Report on  
Applying Agreed-Upon Procedures**

**December 31, 2013**

# St. Lawrence Seaway Pilots' Association

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Independent Accountant's Report on  
Applying Agreed-Upon Procedures

United States Coast Guard  
Great Lakes Pilotage Division

We have performed the procedures enumerated in the accompanying Summary of Agreed-upon Procedures and Results, which were agreed to by the United States Coast Guard solely to assist you in evaluating certain aspects of the expenses incurred by the St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as "District 1" or the "Association") for the year ended December 31, 2013, as explained in Section I of the report. The United States Coast Guard is responsible for evaluating such expenses incurred. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are included in the accompanying Summary of Agreed-Upon Procedures and Results and in the accompanying Summary of Findings and Recommendations, respectively.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on the accounting records. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the United States Coast Guard and the St. Lawrence Seaway Pilots' Association, and is not intended to be and should not be used by anyone other than those specified parties.

*CohnReznick LLP*

Bethesda, Maryland  
September 12, 2014

# St. Lawrence Seaway Pilots' Association

## Summary of Agreed-Upon Procedures and Results

### I. OVERVIEW

The Great Lakes Pilotage Division is responsible for oversight of the St. Lawrence Seaway Pilots' Association, as well as two other pilot associations, which provide piloting services in the Great Lakes region. Included in this oversight function is the responsibility to set pilotage rates based on eligible operating expenses. The agreed-upon procedures listed below are designed to assist the Great Lakes Pilotage Division in determining which expenses meet the eligibility requirements to be included in such rates. Procedures are performed on expenses submitted by the pilot association which they consider to be eligible for ratemaking purposes.

### II. EVALUATION OF REPORTED EXPENSES

#### Procedure:

Obtain a listing of the expenses incurred by District 1 for the year ended December 31, 2013, and perform the following procedures:

1. For each transaction selected for testing, determine if amounts are: a) necessary and reasonable for the provision of pilotage service; b) to be included in pilot compensation or; c) excluded from these categories, using the following information:
  - A. Title 46: Shipping, Part 404-Great Lakes Pilotage Ratemaking, Section 5 Guidelines for the recognition of expenses;
  - B. Federal Register final and interim rulings;
  - C. Previously issued Independent Accountant's Reports on Applying Agreed-Upon Procedures; and
  - D. Discussions with the Director of the United States Coast Guard, Great Lakes Pilotage Division.
2. Segregate each account into 1) general or 2) specific classes.
3. General account classes - a sample of transactions within these accounts will be selected for testing.
  - A. General account classes include:
    - i. Travel expenses
    - ii. Member expenses
    - iii. Repair and maintenance expenses
    - iv. Insurance expenses
    - v. Other operating expenses

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

- B. A sample of general account class transactions will be selected and tested as follows:
  - i. Calculate planning materiality and performance materiality (“PeM” or “75% of planning materiality”), based on total submitted expenses and pilot compensation using industry guidelines.
  - ii. Select all individually significant items in each general account class for testing. Individually transactions greater than 1/3 of PeM are considered individually significant.
  - iii. Using an accounting industry standard sampling form and assessing the risk of material misstatement at high, determine the appropriate sample size with respect to the population of transactions remaining after procedure Bii above.
  - iv. Obtain supporting documentation from the Association for each transaction selected for testing.
  
- 4. Specific accounts class transactions will be tested as follows:
  - A. Pilot compensation and payroll taxes
    - i. Review schedule provided by the District for appropriate classification
    - ii. Agree pilot compensation to the audited financial statements of the District as of December 31, 2013
  
  - B. Depreciation/Auto Leasing/Other
    - iii. Review schedule provided by the District for items that may not be eligible
    - iv. Select material fixed asset additions that are greater than 1/3 of PeM
    - v. Recalculate depreciation expense for each fixed asset addition selected for testing
  
  - C. Payroll (other than pilot compensation) and related expenses
    - i. Review payroll schedule provided by the District for the items that may not be eligible
    - ii. Agree to annual payroll summary register or haphazardly select three employees and agree to employee W-2 or other supporting documentation
    - iii. Recalculate estimated tax calculation and verify appropriate rates are being used
  
  - D. Legal expense
    - i. Review itemized detail for all invoices from the attorney shared by the three Districts
    - ii. Review itemized detail for all invoices from every other attorney identified in the general ledger
  
  - E. Real estate taxes
    - i. Review tax bill for amount, location and tax period
    - ii. Recalculate tax expense based on taxable year

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

- F. Utility expense
    - i. Review general ledger and verify there are no more than 12 monthly transactions during the year
    - ii. Review any transactions in excess of the 12 monthly expected transactions and determine if the expense is appropriate
  - G. Interest expense
    - i. Obtain loan agreement or other documents that provide loan terms, including interest rate
    - ii. Recalculate interest expense based on the principal, interest rate and loan terms
  - H. Pilot subsistence/travel
    - i. Determine that per diem does not exceed 200 days per pilot
    - ii. Where per diem support can be obtained, haphazardly select 5 per diem transactions and agree to supporting expense reimbursement detail
  - I. For all other accounts not tested above
    - i. Review general ledger activity and select any items that appear unusual
    - ii. Select all transactions over 1/3 PeM and obtain supporting documentation
5. Evaluate the results of our test work performed and identify exceptions, if any. Exceptions will be extrapolated to groups, accounts, or by using other measures as deemed appropriate and will result in adjustments to operating expenses. Adjustments will only be recorded for identified misstatements, within a given group, exceeding 3% of planning materiality.

#### Results:

The "Total amount reported" column in the following table represents amounts provided by District 1 from their general ledger for the year ended December 31, 2013. The breakdown of amounts by area was provided by District 1 for information purposes only and was not subject to the procedures above. Exceptions are shown in the "Adjustments" column below. The breakdown of adjustments by area was calculated using the same percentage allocation that was provided by District 1. Each adjustment references the finding number located in the accompanying Summary of Findings and Recommendations, which describes the reasoning for such adjustment.

**St. Lawrence Seaway Pilots' Association**  
**Summary of Agreed-Upon Procedures and Results**

The following are the results of performing such procedures for the year ended December 31, 2013:

	District 1								Adjusted total amount reported
	Area 1	Area 2	Total amount reported	Area 1 adjustments	Area 2 adjustments	Total adjustments	Area 1 adjusted	Area 2 adjusted	
<b>Pilot compensation</b>									
Salaries (D1-13-01)	\$ 1,320,427	\$ 848,059	\$ 2,168,486	\$ 1,855	\$ 1,463	\$ 3,318	\$ 1,322,282	\$ 849,522	\$ 2,171,804
Applicant pilot salaries (D1-13-01)	-	67,531	67,531	-	287	287	-	67,818	67,818
Employee benefits	65,970	41,585	107,555	-	-	-	65,970	41,585	107,555
Dues and subscriptions	2,400	1,800	4,200	-	-	-	2,400	1,800	4,200
<b>Total pilot compensation</b>	<b>\$ 1,388,797</b>	<b>\$ 958,975</b>	<b>\$ 2,347,772</b>	<b>\$ 1,855</b>	<b>\$ 1,750</b>	<b>\$ 3,605</b>	<b>\$ 1,390,652</b>	<b>\$ 960,725</b>	<b>\$ 2,351,377</b>
<b>Operating expenses</b>									
<b>Other pilotage costs</b>									
Pilot subsistence/Travel	\$ 281,488	\$ 168,508	\$ 449,996	\$ -	\$ -	\$ -	\$ 281,488	\$ 168,508	\$ 449,996
License insurance	26,976	25,010	51,986	-	-	-	26,976	25,010	51,986
Payroll taxes (D1-13-01)	65,826	51,244	117,070	(1,855)	(1,750)	(3,605)	63,971	49,494	113,465
Other	6,925	5,460	12,385	-	-	-	6,925	5,460	12,385
<b>Total other pilotage costs</b>	<b>381,215</b>	<b>250,222</b>	<b>631,437</b>	<b>(1,855)</b>	<b>(1,750)</b>	<b>(3,605)</b>	<b>379,360</b>	<b>248,472</b>	<b>627,832</b>
<b>Pilot boat and dispatch costs</b>									
Pilot boat expense	131,193	102,077	233,270	-	-	-	131,193	102,077	233,270
Payroll taxes	9,169	7,230	16,399	-	-	-	9,169	7,230	16,399
<b>Total pilot boat and dispatch costs</b>	<b>140,362</b>	<b>109,307</b>	<b>249,669</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>140,362</b>	<b>109,307</b>	<b>249,669</b>

**St. Lawrence Seaway Pilots' Association**  
**Summary of Agreed-Upon Procedures and Results**

	District 1								
	Area 1	Area 2	Total amount reported	Area 1 adjustments	Area 2 adjustments	Total adjustments	Area 1 adjusted	Area 2 adjusted	Adjusted total amount reported
Administrative expenses									
Legal - general counsel	631	498	1,129	-	-	-	631	498	1,129
Legal - shared counsel (K&L Gates)	12,736	10,040	22,776	-	-	-	12,736	10,040	22,776
Insurance	22,525	17,756	40,281	-	-	-	22,525	17,756	40,281
Employee benefits	11,063	7,868	18,931	-	-	-	11,063	7,868	18,931
Payroll taxes	5,190	4,093	9,282	-	-	-	5,190	4,093	9,282
Other taxes	22,175	17,486	39,661	-	-	-	22,175	17,486	39,661
Travel	524	413	937	-	-	-	524	413	937
Depreciation/Auto leasing/Other	42,285	33,333	75,618	-	-	-	42,285	33,333	75,618
Interest	15,151	11,943	27,094	-	-	-	15,151	11,943	27,094
APA Dues	13,680	10,830	24,510	-	-	-	13,680	10,830	24,510
Dues and subscriptions	280	220	500	-	-	-	280	220	500
Utilities	4,920	3,878	8,798	-	-	-	4,920	3,878	8,798
Salaries	54,153	42,691	96,844	-	-	-	54,153	42,691	96,844
Accounting/Professional fees	5,091	4,009	9,100	-	-	-	5,091	4,009	9,100
Other	8,834	6,954	15,789	-	-	-	8,834	6,954	15,789
<b>Total administrative expenses</b>	<u>219,238</u>	<u>172,012</u>	<u>391,250</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>219,238</u>	<u>172,012</u>	<u>391,250</u>
<b>Total operating expenses</b>	<u>\$ 740,815</u>	<u>\$ 531,541</u>	<u>\$ 1,272,356</u>	<u>\$ (1,855)</u>	<u>\$ (1,750)</u>	<u>\$ (3,605)</u>	<u>\$ 738,960</u>	<u>\$ 529,791</u>	<u>\$ 1,268,751</u>
<b>Total pilot compensation and operating expenses</b>	<u>\$ 2,129,612</u>	<u>\$ 1,490,516</u>	<u>\$ 3,620,128</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,129,612</u>	<u>\$ 1,490,516</u>	<u>\$ 3,620,128</u>

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

#### III. VARIANCE ANALYSIS

##### Procedure:

Obtain a listing of the expenses incurred by District 1 for the years ended December 31, 2009, through December 31, 2013, and perform the following procedures:

1. Segregate accounts into groups based on account description.
2. Compute average of the accounts and groups from 2009 to 2013.
3. Compute difference between the actual balance for each year and the average for each account and group.
4. Compute percentage difference between the actual balance for each year and the average for each account and group.
5. Using the results of procedure number 3 above, identify differences that are greater than 1/3 of PeM. Using the results of procedure number 4 above, identify differences that are greater than 10%. Review remaining account and group analytics and judgmentally determine if any should be selected for additional review.
6. Review the account and group analysis and perform the following procedures:
  - A. Compute pilot compensation as a percentage of revenue;
  - B. Compute pilot boat expense as a percentage of revenue;
  - C. Compute health insurance per pilot;
  - D. Compute travel expense per pilot; and
  - E. Compute training expense per pilot.
7. Obtain explanation and supporting documentation from pilot association personnel, if deemed necessary, to support identified variances and determine if reasonable.
8. Determine whether any instances were identified that led us to believe 2013 expenses were overstated for ratemaking purposes.

##### Results:

No exceptions were noted as a result of performing such procedures.

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

#### IV. INVESTMENT BASE CALCULATION

Procedure:

Prepare the Investment Base Calculation using information obtained from the audited financial statements of St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc., for the year ended December 31, 2013:

	Area 1	Area 2	District 1
<b>Recognized assets</b>			
Total current assets	\$ 983,017	\$ 983,017	\$ 1,675,394
Total current liabilities	87,748	87,748	167,099
Current notes payable	25,908	20,422	46,330
Total property and equipment (NET)	433,514	341,726	775,240
Land	12,322	9,713	22,035
Total other assets	-	-	-
<b>Total recognized assets</b>	<b>1,342,369</b>	<b>1,247,704</b>	<b>2,307,830</b>
<b>Non-recognized assets</b>			
Total investments and special funds	-	-	-
<b>Total non-recognized assets</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total assets</b>			
Total recognized assets	1,342,369	1,247,704	2,307,830
Total non-recognized assets	-	-	-
<b>Total assets</b>	<b>\$ 1,342,369</b>	<b>\$ 1,247,704</b>	<b>\$ 2,307,830</b>
<b>Recognized sources of funds</b>			
Total stockholders' equity	\$ 1,026,743	\$ 809,350	\$ 1,836,093
Long-term debt	250,209	197,232	447,441
Current notes payable	25,908	20,422	46,330
Advances from affiliated companies	-	-	-
Long-term obligations - capital leases	-	-	-
<b>Total recognized sources</b>	<b>1,302,860</b>	<b>1,027,004</b>	<b>2,329,864</b>
<b>Non-recognized sources of funds</b>			
Pension liability	-	-	-
Other non-current liabilities	-	-	-
Deferred federal income taxes	9,608	7,574	17,182
Other deferred credits	-	-	-
<b>Total non-recognized sources</b>	<b>9,608</b>	<b>7,574</b>	<b>17,182</b>
<b>Total sources of funds</b>			
Total recognized sources	1,302,860	1,027,004	2,329,864
Total non-recognized sources	9,608	7,574	17,182
<b>Total sources of funds</b>	<b>\$ 1,312,468</b>	<b>\$ 1,034,578</b>	<b>\$ 2,347,046</b>

Results:

No exceptions were noted as a result of performing such procedures.

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

#### V. COMPARISON OF PILOT ASSOCIATION ACTIVITIES

##### Procedure:

Obtain a listing of the expenses incurred by St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as "District 1"), Lakes Pilots Association, Inc. ("District 2") and Western Great Lakes Pilots Association, LLP ("District 3") for the year ended December 31, 2013, and perform the following procedures:

1. Segregate accounts for each District into four categories: a) Pilot Compensation; b) Other Pilotage Cost; c) Pilot Boat and Dispatch Cost; and d) Administrative Expenses.
2. For each district, compare 2013 expenses and the percentage of each expense, to total district revenue.
3. Perform an analysis of the significant cost categories incurred by the Districts and provide a summary of the composition of the following categories:
  - A. Pilot compensation and payroll taxes,
  - B. Pilot subsistence/travel,
  - C. Pilot boat and dispatch costs,
  - D. Cost associated with affiliated entities, and
  - E. Administrative expenses,
    - i. Legal, accounting and professional fees,
    - ii. Office rent, and
    - iii. Depreciation/auto leasing/other.

**St. Lawrence Seaway Pilots' Association**  
**Summary of Agreed-Upon Procedures and Results**

**Results:**

The following are the results of performing such procedures for the year ended December 31, 2013:

	District 1		District 2		District 3		Total	
Total revenue	<u>\$ 3,694,379</u>		<u>\$ 3,607,407</u>		<u>\$ 4,551,550</u>		<u>\$ 11,853,336</u>	
	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue
<b>Pilot compensation</b>								
Salaries	\$ 2,171,804	58.79%	\$ 1,576,940	43.71%	\$ 1,964,539	43.16%	\$ 5,713,283	48.20%
Applicant pilot salaries	67,818	1.84%	57,991	1.61%	60,000	1.32%	185,809	1.57%
Employee benefits	107,555	2.91%	475,157	13.17%	396,065	8.70%	978,777	8.26%
Applicant pilot employee benefits	-	0.00%	17,882	0.50%	22,022	0.48%	39,904	0.34%
Dues and Subscriptions	4,200	0.11%	2,785	0.08%	5,700	0.13%	12,685	0.11%
<b>Total pilot compensation</b>	<u>\$ 2,351,377</u>	<u>63.65%</u>	<u>\$ 2,130,755</u>	<u>59.07%</u>	<u>\$ 2,448,326</u>	<u>53.79%</u>	<u>\$ 6,930,458</u>	<u>58.47%</u>
<b>Operating expenses</b>								
<b>Other pilotage costs</b>								
Pilot subsistence/Travel	\$ 449,996	12.18%	\$ 210,410	5.83%	\$ 443,728	9.75%	\$ 1,104,134	9.31%
License insurance	51,986	1.41%	15,420	0.43%	18,465	0.41%	85,871	0.72%
Payroll taxes	113,465	3.07%	112,328	3.11%	138,485	3.04%	364,278	3.07%
Other	12,385	0.34%	82,553	2.29%	20,885	0.46%	115,823	0.98%
<b>Total other pilotage costs</b>	<u>627,832</u>	<u>16.97%</u>	<u>420,711</u>	<u>11.65%</u>	<u>621,563</u>	<u>13.65%</u>	<u>1,670,106</u>	<u>14.08%</u>
<b>Pilot boat and dispatching costs</b>								
Pilot boat costs	233,270	6.31%	357,341	9.91%	580,471	12.75%	1,171,082	9.88%
Dispatching costs	-	0.00%	17,700	0.49%	187,254	4.11%	204,954	1.73%
Employee benefits	-	0.00%	151,662	4.20%	-	0.00%	151,662	1.28%
Payroll taxes	16,399	0.44%	20,790	0.58%	20,907	0.46%	58,096	0.49%
<b>Total pilot boat and dispatch costs</b>	<u>249,669</u>	<u>6.76%</u>	<u>547,493</u>	<u>15.17%</u>	<u>788,632</u>	<u>17.33%</u>	<u>1,585,794</u>	<u>13.38%</u>

**St. Lawrence Seaway Pilots' Association**  
**Summary of Agreed-Upon Procedures and Results**

	District 1		District 2		District 3		Total	
Total revenue	<u>\$ 3,694,379</u>		<u>\$ 3,607,407</u>		<u>\$ 4,551,550</u>		<u>\$ 11,853,336</u>	
	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue
Administrative expenses								
Legal - general counsel	1,129	0.03%	8,536	0.24%	756	0.02%	10,421	0.09%
Legal - shared counsel (K&L Gates)	22,776	0.62%	18,260	0.51%	27,014	0.59%	68,050	0.57%
Legal - USCG litigation	-	0.00%	577	0.02%	-	0.00%	577	0.00%
Office rent	-	0.00%	65,688	1.82%	9,900	0.22%	75,588	0.64%
Insurance	40,281	1.09%	17,031	0.47%	10,797	0.24%	68,109	0.57%
Employee benefits	18,931	0.51%	50,564	1.40%	164,003	3.60%	233,498	1.97%
Payroll taxes	9,282	0.25%	12,248	0.34%	13,696	0.30%	35,226	0.30%
Other taxes	39,661	1.07%	37,029	1.03%	1,844	0.04%	78,534	0.66%
Travel	937	0.03%	-	0.00%	-	0.00%	937	0.01%
Depreciation/Auto leasing/Other	75,618	2.05%	41,412	1.15%	32,316	0.71%	149,346	1.26%
Interest	27,094	0.73%	8,598	0.24%	3,204	0.07%	38,896	0.33%
APA Dues	24,510	0.66%	20,520	0.57%	25,194	0.55%	70,224	0.59%
Dues and subscriptions	500	0.01%	-	0.00%	-	0.00%	500	0.00%
Utilities	8,798	0.24%	35,775	0.99%	43,563	0.96%	88,136	0.74%
Salaries	96,844	2.62%	106,582	2.95%	118,923	2.61%	322,349	2.72%
Accounting/Professional fees	9,100	0.25%	23,234	0.64%	27,576	0.61%	59,910	0.51%
Pilot training	-	0.00%	-	0.00%	-	0.00%	-	0.00%
Other	15,789	0.43%	24,395	0.68%	15,012	0.33%	55,196	0.47%
Total administrative expenses	<u>391,250</u>	<u>10.60%</u>	<u>470,449</u>	<u>13.03%</u>	<u>493,798</u>	<u>10.85%</u>	<u>1,355,497</u>	<u>11.44%</u>
Total operating expenses	<u>\$ 1,268,751</u>	<u>34.34%</u>	<u>\$ 1,438,653</u>	<u>39.87%</u>	<u>\$ 1,903,993</u>	<u>41.83%</u>	<u>\$ 4,611,397</u>	<u>38.90%</u>
Total pilot compensation and operating expenses	<u>\$ 3,620,128</u>	<u>97.99%</u>	<u>\$ 3,569,408</u>	<u>98.95%</u>	<u>\$ 4,352,319</u>	<u>95.62%</u>	<u>\$ 11,541,855</u>	<u>97.37%</u>

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

#### Pilot Compensation and Payroll Taxes

- District 1: Pilots were compensated through capital draws based on available funds. Therefore, pilot salary expenses are not recorded in the audited financial statements. All capital drawings have been allocated to pilot compensation or other expenses as deemed appropriate. The pilots were responsible for paying payroll taxes within their personal tax filing. The district did not record a 'self-employment tax equivalent' in the Statement of Pilots' Capital, in its audited financial statements for the year ended December 31, 2013; however, a pilot payroll tax expense was reported by the district. This amount was computed by multiplying total pilot advances by the IRS standard self-employment tax rate of 15.3%, consisting of 12.4% for social security and 2.9% for Medicare, up to \$113,700. Compensation in excess of \$113,700 is subject to the 2.9% Medicare tax only. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.
- District 2: Pilots were compensated on a 'per available day' basis at either \$200 or \$150 per day. Pilots also received other special compensation payments as determined during the year. Payroll taxes were computed and recorded by the association based on IRS guidelines.
- District 3: Pilots were compensated on a 'per available day' basis at an agreed-upon daily rate. The pilots also receive distributions, which are included in pilot compensation for the purposes of this report. The pilots were responsible for paying payroll taxes within their personal tax filing. Therefore, payroll taxes on pilot compensation were not recorded by the Association. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.

#### Pilot Subsistence/Travel

- District 1: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.
- District 2: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.
- District 3: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately

## **St. Lawrence Seaway Pilots' Association**

### **Summary of Agreed-Upon Procedures and Results**

200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.

#### Pilot Boat and Dispatch Costs

- District 1: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. District 1 did not incur dispatch charges, as dispatching was provided by the Canadian Great Lakes Pilotage Authority in exchange for pilot boat services.
- District 2: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. This District provided pilot boat services to its own pilots, as well as pilots from District 3 and Canada. Total expenses incurred were reduced by the revenue incurred from these services. This District also incurred dispatch expenses.
- District 3: This District received pilot boat services from several entities at its various ports, including District 2. This District employed dispatchers to handle its dispatch needs.

#### Costs Associated with Affiliated Entities

- District 1: Seaway Pilot Inc. is an affiliate of St. Lawrence Seaway Pilots' Association and provides services such as pilot boat operations, bookkeeping and administration services, and equipment rental. Expenses incurred by St. Lawrence Seaway Pilots' Association related to these services were eliminated for these agreed-upon procedures.
- District 2: This District leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually. In addition to the required monthly lease payments, the lease agreement requires payments of utilities, maintenance and property taxes.
- District 3: This District did not enter into transactions with or make payments to affiliated entities.

#### Administrative Expense

##### Legal, Accounting and Professional Fees:

- District 1: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.
- District 2: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. During 2013, the District incurred legal expenses related to ongoing litigation with the United States Coast Guard. The

## St. Lawrence Seaway Pilots' Association

### Summary of Agreed-Upon Procedures and Results

District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 3: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

#### Office Rent:

District 1: This District did not incur office rent expense. It operated in a building owned by Seaway Pilot Inc.

District 2: This district leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually.

District 3: This District leased office space from an unrelated party on a month-to-month basis at an amount equal to \$9,900 annually.

#### Depreciation/Auto Leasing/Other:

District 1: This District incurred depreciation on an office building, pilot boats and various pieces of equipment.

District 2: This District incurred depreciation on pilot boats, a housing location at one port, and various pieces of equipment. The district also entered into automobile lease agreements.

District 3: This District incurred depreciation on equipment and vehicles.

## VI. RECOMMENDED GENERAL LEDGER ACCOUNTS

#### Procedure:

Recommend a list of general ledger accounts for use by each Association.

#### Results:

As a result of performing the aforementioned agreed-upon procedures, we recommend the Districts incorporate the account groupings listed in Procedures I and III into the financial data provided to the Great Lakes Pilotage Division for analysis, understanding that more detailed subaccounts would be necessary to accurately classify expenses incurred.

**St. Lawrence Seaway Pilots' Association**  
**Summary of Findings and Recommendations**

The following findings detail adjustments necessary for ratemaking purposes, as identified in section II of the previous report.

Finding Number: D1-13-01

Finding Title: Pilot Salaries and Payroll Taxes

Condition:

The Association recorded excess payroll taxes for pilot compensation.

Criteria:

Federal Register, Vol. 70, No. 46, section 12091 dated March 10, 2005 allows for estimated Social Security and Medicare taxes to be recorded on behalf of the Association when these taxes are incurred by the pilots on their individual tax returns. Note: these estimates are based on taxes that would be incurred by the Association, not what the pilots incur on their own tax returns as a self-employed individual.

Effect:

Operating expenses are overstated.

Cause:

The pilots of the Association are self-employed, therefore they incur these payroll costs on their individual tax returns.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards. Estimates should be based on taxes that would be incurred by the Association and not based on individual self-employment rates.

**Lakes Pilots Association, Inc.  
Contract # GS-23F-0124M**

**Independent Accountant's Report on  
Applying Agreed-Upon Procedures**

**December 31, 2013**

**Lakes Pilots Association, Inc.**

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Independent Accountant's Report on  
Applying Agreed-Upon Procedures

United States Coast Guard  
Great Lakes Pilotage Division

We have performed the procedures enumerated in the accompanying Summary of Agreed-upon Procedures and Results, which were agreed to by the United States Coast Guard solely to assist you in evaluating certain aspects of the expenses incurred by the Lakes Pilots Association, Inc. ("District 2" or the "Association") for the year ended December 31, 2013, as explained in Section I of the report. The United States Coast Guard is responsible for evaluating such expenses incurred. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are included in the accompanying Summary of Agreed-Upon Procedures and Results and in the accompanying Summary of Findings and Recommendations, respectively.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on the accounting records. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the United States Coast Guard and the Lakes Pilots Association, Inc., and is not intended to be and should not be used by anyone other than those specified parties.



Bethesda, Maryland  
September 12, 2014

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

#### I. OVERVIEW

The Great Lakes Pilotage Division is responsible for oversight of the Lakes Pilots Association, Inc., as well as two other pilot associations, which provide piloting services in the Great Lakes region. Included in this oversight function is the responsibility to set pilotage rates based on eligible operating expenses. The agreed-upon procedures listed below are designed to assist the Great Lakes Pilotage Division in determining which expenses meet the eligibility requirements to be included in such rates. Procedures are performed on expenses submitted by the pilot association which they consider to be eligible for ratemaking purposes.

#### II. EVALUATION OF REPORTED EXPENSES

##### Procedure:

Obtain a listing of the expenses submitted by District 2 for the year ended December 31, 2013, and perform the following procedures:

1. For each transaction selected for testing, determine if amounts are a) necessary and reasonable for the provision of pilotage service; b) to be included in pilot compensation or; c) excluded from these categories, using the following information:
  - A. Title 46: Shipping, Part 404-Great Lakes Pilotage Ratemaking, Section 5 Guidelines for the recognition of expenses;
  - B. Federal Register final and interim rulings;
  - C. Previously issued Independent Accountant's Reports on Applying Agreed-Upon Procedures; and
  - D. Discussions with the Director of the United States Coast Guard, Great Lakes Pilotage Division.
2. Segregate each account into 1) general or 2) specific classes.
3. General account classes - a sample of transactions within these accounts will be selected for testing.
  - A. General account classes include:
    - i. Travel expenses
    - ii. Pilot boat and dispatch cost
    - iii. Insurance expenses
    - iv. Other operating expenses

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

- B. A sample of general account class transactions will be selected and tested as follows:
  - i. Calculate planning materiality and performance materiality (“PeM” or “75% of planning materiality”), based on total submitted expenses and pilot compensation using industry guidelines.
  - ii. Select all individually significant items in each general account class for testing. Individually transactions greater than 1/3 of PeM are considered individually significant.
  - iii. Using an accounting industry standard sampling form and assessing the risk of material misstatement at high, determine the appropriate sample size with respect to the population of transactions remaining after procedure Bii above.
  - iv. Obtain supporting documentation from the Association for each transaction selected for testing.
  
- 4. Specific accounts class transactions will be tested as follows:
  - A. Pilot compensation and payroll taxes
    - i. Review schedule provided by the District for appropriate classification
    - ii. Agree pilot compensation to the audited financial statements of the District as of December 31, 2013
  
  - B. Depreciation expense
    - i. Review schedule provided by the District for items that may not be eligible
    - ii. Select material fixed asset additions that are greater than 1/3 of PeM
    - iii. Recalculate depreciation expense for each fixed asset addition selected for testing
  
  - C. Payroll (other than pilot compensation) and related expenses
    - i. Review payroll schedule provided by the District for the items that may not be eligible
    - ii. Agree to annual payroll summary register or select three employees and agree to employee W-2
    - iii. Recalculate estimated tax calculation and verify appropriate rates are being used
  
  - D. Legal expense
    - i. Review itemized detail for all invoices from the attorney shared by the three Districts
    - ii. Review itemized detail for all invoices from every other attorney identified in the general ledger
  
  - E. Real estate taxes
    - i. Review tax bill for amount, location and tax period
    - ii. Recalculate tax expense based on taxable year
  
  - F. Pilot subsistence/travel
    - i. Determine that per diem does not exceed 200 days per pilot

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

- ii. Where per diem support can be obtained, haphazardly select 5 per diem transactions and agree to supporting expense reimbursement detail
- G. Utility expense
- i. Review general ledger and verify there are no more than 12 monthly transactions during the year
  - ii. Review any transactions in excess of the 12 monthly expected transactions and determine if the expense is appropriate
- H. Office rent expense
- i. Obtain signed lease agreement and recalculate the expense based on the terms of the lease
  - ii. For lease agreements with affiliated entities, CFR Part 404.5 (3) will be applied, stating that “in the absence of a comparable market, lease costs are recognized for ratemaking purposes to the extent that they conform to depreciation plus an allowance for return on investment.” In lieu of depreciation, actual annual expenses incurred in conjunction with purchase and maintenance of the land will be determined. Return on investment will be determined using the Moody's Corporate Bond AAA index as of December 31, 2013, or 4.57%
- I. Interest expense
- i. Obtain loan agreement or other documents that provide loan terms, including interest rate
  - ii. Recalculate interest expense based on the principal, interest rate and loan terms
- J. For all other accounts not tested above
- i. Review general ledger activity and select any items that appear unusual
  - ii. Select all transactions over 1/3 PeM and obtain supporting documentation
5. Evaluate the results of our test work performed and identify exceptions, if any. Exceptions will be extrapolated to groups, accounts, or by using other measures as deemed appropriate and will result in adjustments to operating expenses. Adjustments will only be recorded for identified misstatements, within a given group, exceeding 3% of planning materiality.

#### Results:

The “Total amount reported” column in the following table represents amounts provided by District 2 from their general ledger for the year ended December 31, 2013. The breakdown of amounts by area was provided by District 2 for information purposes only and was not subject to the procedures above. Exceptions are shown in the “Adjustments” column below. The breakdown of adjustments by area was calculated using the same percentage allocation that was provided by District 2. Each adjustment references the finding number located in the accompanying Summary of Findings and Recommendations, which describes the reasoning for such adjustment.

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

The following are the results of performing such procedures for the year ended December 31, 2013:

			District 2					Adjusted total amount reported	
	Area 4	Area 5	Total amount reported	Area 4 adjustments	Area 5 adjustments	Total adjustments	Area 4 adjusted		Area 5 adjusted
<b>Pilot compensation</b>									
Salaries	\$ 630,776	\$ 946,164	\$ 1,576,940 *	\$ -	\$ -	\$ -	\$ 630,776	\$ 946,164	\$ 1,576,940
Applicant pilot salaries	23,197	34,795	57,991	-	-	-	23,197	34,795	57,991
Employee benefits	190,063	285,094	475,157	-	-	-	190,063	285,094	475,157
Applicant pilot employee benefits	7,153	10,729	17,882	-	-	-	7,153	10,729	17,882
Dues and subscriptions	1,114	1,671	2,785	-	-	-	1,114	1,671	2,785
<b>Total pilot compensation</b>	<b>\$ 852,302</b>	<b>\$ 1,278,453</b>	<b>\$ 2,130,755</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 852,302</b>	<b>\$ 1,278,453</b>	<b>\$ 2,130,755</b>
<b>Operating expenses</b>									
<b>Other pilotage costs</b>									
Pilot subsistence/Travel	\$ 84,164	\$ 126,246	\$ 210,410	\$ -	\$ -	\$ -	\$ 84,164	\$ 126,246	\$ 210,410
License insurance	6,168	9,252	15,420	-	-	-	6,168	9,252	15,420
Payroll taxes	44,931	67,397	112,328	-	-	-	44,931	67,397	112,328
Other	33,021	49,532	82,553	-	-	-	33,021	49,532	82,553
<b>Total other pilotage costs</b>	<b>168,284</b>	<b>252,427</b>	<b>420,711</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>168,284</b>	<b>252,427</b>	<b>420,711</b>
<b>Pilot boat and dispatch costs</b>									
Pilot boat costs	142,936	214,405	357,341	-	-	-	142,936	214,405	357,341
Dispatch costs	7,080	10,620	17,700	-	-	-	7,080	10,620	17,700
Employee benefits	60,665	90,997	151,662	-	-	-	60,665	90,997	151,662
Payroll taxes	8,316	12,474	20,790	-	-	-	8,316	12,474	20,790
<b>Total pilot boat and dispatch costs</b>	<b>218,997</b>	<b>328,496</b>	<b>547,493</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>218,997</b>	<b>328,496</b>	<b>547,493</b>

\*Includes \$36,000 of dividends that were not subject to the agreed-upon procedures in Section II

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

			District 2					Adjusted total amount reported	
	Area 4	Area 5	Total amount reported	Area 4 adjustments	Area 5 adjustments	Total adjustments	Area 4 adjusted		Area 5 adjusted
Administrative expenses									
Legal - general counsel	3,414	5,122	8,536	-	-	-	3,414	5,122	8,536
Legal - shared counsel (K&L Gates)	7,304	10,956	18,260	-	-	-	7,304	10,956	18,260
Legal - USCG litigation	231	346	577	-	-	-	231	346	577
Office rent	26,275	39,413	65,688	-	-	-	26,275	39,413	65,688
Insurance (D2-13-01)	9,175	13,762	22,937	(2,362)	(3,544)	(5,906)	6,812	10,219	17,031
Employee benefits (D2-13-01)	20,586	30,879	51,465	(360)	(541)	(901)	20,226	30,338	50,564
Payroll taxes	4,899	7,349	12,248	-	-	-	4,899	7,349	12,248
Other taxes	14,812	22,217	37,029	-	-	-	14,812	22,217	37,029
Depreciation/Auto leasing/Other (D2-13-02)	22,956	34,434	57,390	(6,391)	(9,587)	(15,978)	16,565	24,847	41,412
Interest	3,439	5,159	8,598	-	-	-	3,439	5,159	8,598
APA Dues	8,208	12,312	20,520	-	-	-	8,208	12,312	20,520
Utilities	14,310	21,465	35,775	-	-	-	14,310	21,465	35,775
Salaries	42,633	63,949	106,582	-	-	-	42,633	63,949	106,582
Accounting/Professional fees	9,294	13,940	23,234	-	-	-	9,294	13,940	23,234
Pilot training	-	-	-	-	-	-	-	-	-
Other	9,757	14,638	24,395	-	-	-	9,757	14,638	24,395
<b>Total administrative expenses</b>	<b>197,293</b>	<b>295,941</b>	<b>493,234</b>	<b>(9,114)</b>	<b>(13,671)</b>	<b>(22,785)</b>	<b>188,179</b>	<b>282,270</b>	<b>470,449</b>
<b>Total operating expenses</b>	<b>\$ 584,574</b>	<b>\$ 876,864</b>	<b>\$ 1,461,438</b>	<b>\$ (9,113)</b>	<b>\$ (13,671)</b>	<b>\$ (22,785)</b>	<b>\$ 575,460</b>	<b>\$ 863,193</b>	<b>\$ 1,438,653</b>
<b>Total pilot compensation and operating expenses</b>	<b>\$ 1,436,876</b>	<b>\$ 2,155,317</b>	<b>\$ 3,592,193</b>	<b>\$ (9,114)</b>	<b>\$ (13,671)</b>	<b>\$ (22,785)</b>	<b>\$ 1,427,762</b>	<b>\$ 2,141,646</b>	<b>\$ 3,569,408</b>

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

#### III. VARIANCE ANALYSIS

##### Procedure:

Obtain a listing of the expenses incurred by District 2 for the years ended December 31, 2009, through December 31, 2013, and perform the following procedures:

1. Segregate accounts into groups based on account description.
2. Compute average of the accounts and groups from 2009 to 2013.
3. Compute difference between the actual balance for each year and the average for each account and group.
4. Compute percentage difference between the actual balance for each year and the average for each account and group.
5. Using the results of procedure number 3 above, identify differences that are greater than 1/3 of PeM. Using the results of procedure number 4 above, identify differences that are greater than 10%. Review remaining account and group analytics and judgmentally determine if any should be selected for additional review.
6. Review the account and group analysis and perform the following procedures:
  - A. Compute pilot compensation as a percentage of revenue;
  - B. Compute pilot boat expense as a percentage of revenue;
  - C. Compute health insurance per pilot;
  - D. Compute travel expense per pilot; and
  - E. Compute training expense per pilot.
7. Obtain explanation and supporting documentation from pilot association personnel, if deemed necessary, to support identified variances and determine if reasonable.
8. Determine whether any instances were identified that led us to believe 2013 expenses were overstated for ratemaking purposes.

##### Results:

No exceptions were noted as a result of performing such procedures.

**Lakes Pilots Association, Inc.**

**Summary of Agreed-Upon Procedures and Results**

**IV. INVESTMENT BASE CALCULATION**

**Procedure:**

Prepare the Investment Base Calculation using information obtained from the audited financial statements of Lakes Pilots Association, Inc. for the year ended December 31, 2013:

	Area 4	Area 5	District 2
<b>Recognized assets</b>			
Total current assets	\$ 611,820	\$ 917,731	\$ 1,529,551
Total current liabilities	606,762	910,143	1,516,905
Current notes payable	35,508	53,263	88,771
Total property and equipment (NET)	410,724	616,087	1,026,811
Land	-	-	-
Total other assets	60,560	90,840	151,400
<b>Total recognized assets</b>	<b>511,850</b>	<b>767,778</b>	<b>1,279,628</b>
<b>Non-recognized assets</b>			
Total investments and special funds	-	-	-
<b>Total non-recognized assets</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total assets</b>			
Total recognized assets	511,850	767,778	1,279,628
Total non-recognized assets	-	-	-
<b>Total assets</b>	<b>\$ 511,850</b>	<b>\$ 767,778</b>	<b>\$ 1,279,628</b>
<b>Recognized sources of funds</b>			
Total stockholders' equity	\$ 96,800	\$ 145,201	\$ 242,001
Long-term debt	379,542	569,314	948,856
Current notes payable	35,508	53,263	88,771
Advances from affiliated companies	-	-	-
Long-term obligations - capital leases	-	-	-
<b>Total recognized sources</b>	<b>511,850</b>	<b>767,778</b>	<b>1,279,628</b>
<b>Non-recognized sources of funds</b>			
Pension liability	-	-	-
Other non-current liabilities	-	-	-
Deferred federal income taxes	-	-	-
Other deferred credits	-	-	-
<b>Total non-recognized sources</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total sources of funds</b>			
Total recognized sources	511,850	767,778	1,279,628
Total non-recognized sources	-	-	-
<b>Total sources of funds</b>	<b>\$ 511,850</b>	<b>\$ 767,778</b>	<b>\$ 1,279,628</b>

**Results:**

No exceptions were noted as a result of performing such procedures.

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

#### V. COMPARISON OF PILOT ASSOCIATION ACTIVITIES

##### Procedure:

Obtain a listing of the expenses incurred by St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as District 1), District 2 and Western Great Lakes Pilots Association, LLP ("District 3") for the year ended December 31, 2013 and perform the following procedures:

1. Segregate accounts for each District into four categories: a) Pilot Compensation, b) Other Pilotage Cost, c) Pilot Boat and Dispatch Cost and d) Administrative Expenses.
2. For each district, compare 2013 expenses and the percentage of each expense, to total district revenue.
3. Perform an analysis of the significant cost categories incurred by the Districts and provide a summary of the composition of the following categories:
  - A. Pilot compensation and payroll taxes,
  - B. Pilot subsistence/travel,
  - C. Pilot boat and dispatch costs,
  - D. Cost associated with affiliated entities, and
  - E. Administrative expenses,
    - i. Legal, accounting and professional fees,
    - ii. Office rent, and
    - iii. Depreciation/auto leasing/other.

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

#### Results:

The following are the results of performing such procedures December 31, 2013:

	District 1		District 2		District 3		Total	
Total revenue	\$ 3,694,379		\$ 3,607,407		\$ 4,551,550		\$ 11,853,336	
	Adjusted amount	% of district revenue						
Pilot compensation								
Salaries	\$ 2,171,804	58.79%	\$ 1,576,940	43.71%	\$ 1,964,539	43.16%	\$ 5,713,283	48.20%
Applicant pilot salaries	67,818	1.84%	57,991	1.61%	60,000	1.32%	185,809	1.57%
Employee benefits	107,555	2.91%	475,157	13.17%	396,065	8.70%	978,777	8.26%
Applicant pilot employee benefits	-	0.00%	17,882	0.50%	22,022	0.48%	39,904	0.34%
Dues and Subscriptions	4,200	0.11%	2,785	0.08%	5,700	0.13%	12,685	0.11%
Total pilot compensation	<u>\$ 2,351,377</u>	<u>63.65%</u>	<u>\$ 2,130,755</u>	<u>59.07%</u>	<u>\$ 2,448,326</u>	<u>53.79%</u>	<u>\$ 6,930,458</u>	<u>58.47%</u>
Operating expenses								
Other pilotage costs								
Pilot subsistence/Travel	\$ 449,996	12.18%	\$ 210,410	5.83%	\$ 443,728	9.75%	\$ 1,104,134	9.31%
License insurance	51,986	1.41%	15,420	0.43%	18,465	0.41%	85,871	0.72%
Payroll taxes	113,465	3.07%	112,328	3.11%	138,485	3.04%	364,278	3.07%
Other	12,385	0.34%	82,553	2.29%	20,885	0.46%	115,823	0.98%
Total other pilotage costs	<u>627,832</u>	<u>16.97%</u>	<u>420,711</u>	<u>11.65%</u>	<u>621,563</u>	<u>13.65%</u>	<u>1,670,106</u>	<u>14.08%</u>
Pilot boat and dispatching costs								
Pilot boat costs	233,270	6.31%	357,341	9.91%	580,471	12.75%	1,171,082	9.88%
Dispatching costs	-	0.00%	17,700	0.49%	187,254	4.11%	204,954	1.73%
Employee benefits	-	0.00%	151,662	4.20%	-	0.00%	151,662	1.28%
Payroll taxes	16,399	0.44%	20,790	0.58%	20,907	0.46%	58,096	0.49%
Total pilot boat and dispatch costs	<u>249,669</u>	<u>6.76%</u>	<u>547,493</u>	<u>15.17%</u>	<u>788,632</u>	<u>17.33%</u>	<u>1,585,794</u>	<u>13.38%</u>

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

	District 1		District 2		District 3		Total	
Total revenue	\$ 3,694,379		\$ 3,607,407		\$ 4,551,550		\$ 11,853,336	
	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue
Administrative expenses								
Legal - general counsel	1,129	0.03%	8,536	0.24%	756	0.02%	10,421	0.09%
Legal - shared counsel (K&L Gates)	22,776	0.62%	18,260	0.51%	27,014	0.59%	68,050	0.57%
Legal - USCG litigation	-	0.00%	577	0.02%	-	0.00%	577	0.00%
Office rent	-	0.00%	65,688	1.82%	9,900	0.22%	75,588	0.64%
Insurance	40,281	1.09%	17,031	0.47%	10,797	0.24%	68,109	0.57%
Employee benefits	18,931	0.51%	50,564	1.40%	164,003	3.60%	233,498	1.97%
Payroll taxes	9,282	0.25%	12,248	0.34%	13,696	0.30%	35,226	0.30%
Other taxes	39,661	1.07%	37,029	1.03%	1,844	0.04%	78,534	0.66%
Travel	937	0.03%	-	0.00%	-	0.00%	937	0.01%
Depreciation/Auto leasing/Other	75,618	2.05%	41,412	1.15%	32,316	0.71%	149,346	1.26%
Interest	27,094	0.73%	8,598	0.24%	3,204	0.07%	38,896	0.33%
APA Dues	24,510	0.66%	20,520	0.57%	25,194	0.55%	70,224	0.59%
Dues and subscriptions	500	0.01%	-	0.00%	-	0.00%	500	0.00%
Utilities	8,798	0.24%	35,775	0.99%	43,563	0.96%	88,136	0.74%
Salaries	96,844	2.62%	106,582	2.95%	118,923	2.61%	322,349	2.72%
Accounting/Professional fees	9,100	0.25%	23,234	0.64%	27,576	0.61%	59,910	0.51%
Pilot training	-	0.00%	-	0.00%	-	0.00%	-	0.00%
Other	15,789	0.43%	24,395	0.68%	15,012	0.33%	55,196	0.47%
<b>Total administrative expenses</b>	<b>391,250</b>	<b>10.60%</b>	<b>470,449</b>	<b>13.03%</b>	<b>493,798</b>	<b>10.85%</b>	<b>1,355,497</b>	<b>11.44%</b>
<b>Total operating expenses</b>	<b>\$ 1,268,751</b>	<b>34.34%</b>	<b>\$ 1,438,653</b>	<b>39.87%</b>	<b>\$ 1,903,993</b>	<b>41.83%</b>	<b>\$ 4,611,397</b>	<b>38.90%</b>
<b>Total pilot compensation and operating expenses</b>	<b>\$ 3,620,128</b>	<b>97.99%</b>	<b>\$ 3,569,408</b>	<b>98.95%</b>	<b>\$ 4,352,319</b>	<b>95.62%</b>	<b>\$ 11,541,855</b>	<b>97.37%</b>

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

#### Pilot Compensation and Payroll Taxes

- District 1: Pilots were compensated through capital draws based on available funds. Therefore, pilot salary expenses are not recorded in the audited financial statements. All capital drawings have been allocated to pilot compensation or other expenses as deemed appropriate. The pilots were responsible for paying payroll taxes within their personal tax filing. The district did not record a 'self-employment tax equivalent' in the Statement of Pilots' Capital, in its audited financial statements for the year ended December 31, 2013; however, a pilot payroll tax expense was reported by the district. This amount was computed by multiplying total pilot advances by the IRS standard self-employment tax rate of 15.3%, consisting of 12.4% for social security and 2.9% for Medicare, up to \$113,700. Compensation in excess of \$113,700 is subject to the 2.9% Medicare tax only. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.
- District 2: Pilots were compensated on a 'per available day' basis at either \$200 or \$150 per day. Pilots also received other special compensation payments as determined during the year. Payroll taxes were computed and recorded by the association based on IRS guidelines.
- District 3: Pilots were compensated on a 'per available day' basis at an agreed-upon daily rate. The pilots also receive distributions, which are included in pilot compensation for the purposes of this report. The pilots were responsible for paying payroll taxes within their personal tax filing. Therefore, payroll taxes on pilot compensation were not recorded by the Association. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.

#### Pilot Subsistence/Travel

- District 1: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.
- District 2: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.
- District 3: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.

#### Pilot Boat and Dispatch Costs

- District 1: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. District 1 did not incur dispatch charges, as dispatching was provided by the Canadian Great Lakes Pilotage Authority in exchange for pilot boat services.
- District 2: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. This District provided pilot boat services to its own pilots, as well as pilots from District 3 and Canada. Total expenses incurred were reduced by the revenue incurred from these services. This District also incurred dispatch expenses.
- District 3: This District received pilot boat services from several entities at its various ports, including District 2. This District employed dispatchers to handle its dispatch needs.

#### Costs Associated with Affiliated Entities

- District 1: Seaway Pilot Inc. is an affiliate of St. Lawrence Seaway Pilots' Association and provides services such as pilot boat operations, bookkeeping and administration services, and equipment rental. Expenses incurred by St. Lawrence Seaway Pilots' Association related to these services were eliminated for these agreed-upon procedures.
- District 2: This District leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually. In addition to the required monthly lease payments, the lease agreement requires payments of utilities, maintenance and property taxes.
- District 3: This District did not enter into transactions with or make payments to affiliated entities.

#### Administrative Expense

##### Legal, Accounting and Professional Fees:

- District 1: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.
- District 2: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. During 2013, the District incurred legal expenses related to ongoing litigation with the United States Coast Guard. The

## Lakes Pilots Association, Inc.

### Summary of Agreed-Upon Procedures and Results

District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 3: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

#### Office Rent:

District 1: This District did not incur office rent expense. It operated in a building owned by Seaway Pilot Inc.

District 2: This district leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually.

District 3: This District leased office space from an unrelated party on a month-to-month basis at an amount equal to \$9,900 annually.

#### Depreciation/Auto Leasing/Other:

District 1: This District incurred depreciation on an office building, pilot boats and various pieces of equipment.

District 2: This District incurred depreciation on pilot boats, a housing location at one port, and various pieces of equipment. The District also entered into automobile lease agreements.

District 3: This District incurred depreciation on equipment and vehicles.

## VI. RECOMMENDED GENERAL LEDGER ACCOUNTS

### Procedure:

Recommend a list of general ledger accounts for use by each Association.

### Results:

As a result of performing the aforementioned agreed-upon procedures, we recommend the Districts incorporate the account groupings listed in Procedures I and III into the financial data provided to the Great Lakes Pilotage Division for analysis, understanding that more detailed subaccounts would be necessary to accurately classify expenses incurred.

**Lakes Pilots Association, Inc.**

**Summary of Findings and Recommendations**

The following findings detail adjustments necessary for ratemaking purposes, as identified in section II of the previous report.

Finding Number: D2-13-01

Finding Title: Insurance and Employee Benefits

Condition:

The Association recorded and paid for cost in 2013 that were incurred in 2012 or will be incurred in 2014.

Criteria:

The scope of this report is that only 2013 expenses are allowable for ratemaking purposes.

Effect:

Operating expenses are overstated.

Cause:

Expenses incurred in 2012 and 2014 were recorded and paid during 2013.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D2-13-02

Finding Title: Depreciation/Auto leasing/Other

Condition:

The Association recorded depreciation expense using an accelerated method of depreciation that is not conformity with generally accepted accounting principles.

Criteria:

The scope of this report is that only 2013 expenses are allowable for ratemaking purposes.

Effect:

Operating expenses are overstated.

Cause:

The scope of this report is that only 2013 expenses are allowable for ratemaking purposes.

**Lakes Pilots Association, Inc.**

**Summary of Findings and Recommendations**

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

**Western Great Lakes Pilots  
Association, LLP  
Contract # GS-23F-0124M**

**Independent Accountant's Report on  
Applying Agreed-Upon Procedures**

**December 31, 2013**

# Western Great Lakes Pilots Association, LLP

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Independent Accountant's Report on  
Applying Agreed-Upon Procedures

United States Coast Guard  
Great Lakes Pilotage Division

We have performed the procedures enumerated in the accompanying Summary of Agreed-upon Procedures and Results, which were agreed to by the United States Coast Guard solely to assist you in evaluating certain aspects of the expenses incurred by the Western Great Lakes Pilots Association, LLP (District 3 or the Association) for the year ended December 31, 2013, as explained in Section I of the report. The United States Coast Guard is responsible for evaluating such expenses incurred. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the specified users of the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are included in the accompanying Summary of Agreed-Upon Procedures and Results and in the accompanying Summary of Findings and Recommendations, respectively.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on the accounting records. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the United States Coast Guard and the Western Great Lakes Pilots Association, LLP, and is not intended to be and should not be used by anyone other than those specified parties.

*CohnReznick LLP*

Bethesda, Maryland  
September 12, 2014

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

#### I. OVERVIEW

The Great Lakes Pilotage Division is responsible for oversight of the Western Great Lakes Pilots Association, LLP, as well as two other pilot associations, which provide piloting services in the Great Lakes region. Included in this oversight function is the responsibility to set pilotage rates based on eligible operating expenses. The agreed-upon procedures listed below are designed to assist the Great Lakes Pilotage Division in determining which expenses meet the eligibility requirements to be included in such rates. Procedures are performed on expenses submitted by the pilot association which they consider to be eligible for ratemaking purposes.

#### II. EVALUATION OF REPORTED EXPENSES

##### Procedure:

Obtain a listing of the expenses submitted by District 3 for the year ended December 31, 2013, and perform the following procedures:

1. For each transaction selected for testing, determine if amounts are a) necessary and reasonable for the provision of pilotage service; b) to be included in pilot compensation or; c) excluded from these categories, using the following information:
  - A. Title 46: Shipping, Part 404-Great Lakes Pilotage Ratemaking, Section 5 Guidelines for the recognition of expenses;
  - B. Federal Register final and interim rulings;
  - C. Previously issued Independent Accountant's Reports on Applying Agreed-Upon Procedures; and
  - D. Discussions with the Director of the United States Coast Guard, Great Lakes Pilotage Division.
2. Segregate each account into 1) general or 2) specific classes.
3. General account classes - a sample of transactions within these accounts will be selected for testing.
  - A. General account classes include:
    - i. Travel expenses
    - ii. Pilot boat and dispatch cost
    - iii. Insurance expenses
    - iv. Other operating expenses

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

- B. A sample of general account class transactions will be selected and tested as follows:
  - i. Calculate planning materiality and performance materiality (“PeM” or “75% of planning materiality”), based on total submitted expenses and pilot compensation using industry guidelines.
  - ii. Select all individually significant items in each general account class for testing. Individually transactions greater than 1/3 of PeM are considered individually significant.
  - iii. Using an accounting industry standard sampling form and assessing the risk of material misstatement at high, determine the appropriate sample size with respect to the population of transactions remaining after procedure Bii above.
  - iv. Obtain supporting documentation from the Association for each transaction selected for testing.
- 4. Specific accounts class transactions will be tested as follows:
  - A. Pilot compensation and payroll taxes
    - i. Review schedule provided by the District for appropriate classification
    - ii. Agree pilot compensation to the audited financial statements of the District as of December 31, 2013
  - B. Depreciation expense
    - i. Review schedule provided by the District for items that may not be eligible
    - ii. Select material fixed asset additions that are greater than 1/3 of PeM
    - iii. Recalculate depreciation expense for each fixed asset addition selected for testing
  - C. Payroll (other than pilot compensation) and related expenses
    - i. Review payroll schedule provided by the District for the items that may not be eligible
    - ii. Agree to annual payroll summary register or haphazardly select three employees and agree to employee W-2
    - iii. Recalculate estimated tax calculation and verify appropriate rates are being used
  - D. Legal expense
    - i. Review itemized detail for all invoices from the attorney shared by the three Districts
    - ii. Review itemized detail for all invoices from every other attorney identified in the general ledger
  - E. Real estate taxes
    - i. Review tax bill for amount, location and tax period
    - ii. Recalculate tax expense based on taxable year
  - F. Utility expense

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

- i. Review general ledger and verify there are no more than 12 monthly transactions during the year
    - ii. Review any transactions in excess of the 12 monthly expected transactions and determine if the expense is appropriate
  - G. Office rent expense
    - i. Obtain signed lease agreement and recalculate the expense based on the terms of the lease
  - H. Interest expense
    - i. Obtain loan agreement or other documents that provide loan terms, including interest rate
    - ii. Recalculate interest expense based on the principal, interest rate and loan terms
  - I. Pilot subsistence/travel
    - i. Determine that per diem does not exceed 200 days per pilot
    - ii. Where per diem support can be obtained, haphazardly select 5 per diem transactions and agree to supporting expense reimbursement detail
  - J. For all other accounts not tested above
    - i. Review general ledger activity and select any items that appear unusual
    - ii. Select all transactions over 1/3 PeM and obtain supporting documentation
5. Evaluate the results of our test work performed and identify exceptions, if any. Exceptions will be extrapolated to groups, accounts, or by using other measures as deemed appropriate and will result in adjustments to operating expenses. Adjustments will only be recorded for identified misstatements, within a given group, exceeding 3% of planning materiality.

#### Results:

The "Total amount reported" column in the following table represents amounts provided by District 3 from their general ledger for the year ended December 31, 2013. The breakdown of amounts by area was provided by District 3 for information purposes only and was not subject to the procedures above. Exceptions are shown in the "Adjustments" column below. The breakdown of adjustments by area was calculated using the same percentage allocation that was provided by District 3. Each adjustment references the finding number located in the accompanying Summary of Findings and Recommendations, which describes the reasoning for such adjustment.

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upn Procedures and Results

The following are the results of performing such procedures for the year ended December 31, 2013:

	District 3											
	Area 6	Area 7	Area 8	Total amount reported	Area 6 adjustments	Area 7 adjustments	Area 8 adjustments	Total adjustments	Area 6 adjusted	Area 7 adjusted	Area 8 adjusted	Adjusted total amount reported
<b>Pilot compensation</b>												
Salaries (D3-13-01)	\$ 1,002,520	\$ 556,956	\$ 668,347	\$ 2,227,823 *	\$ (118,478)	\$ (65,821)	\$ (78,985)	\$ (263,284)	\$ 884,042	\$ 491,135	\$ 589,362	\$ 1,964,539
Applicant pilot salaries	27,000	15,000	18,000	60,000	-	-	-	-	27,000	15,000	18,000	60,000
Employee benefits	178,229	99,016	118,820	396,065	-	-	-	-	178,229	99,016	118,820	396,065
Applicant pilot employee benefits	9,910	5,506	6,606	22,022	-	-	-	-	9,910	5,506	6,606	22,022
Dues and subscriptions (D3-13-02)	-	-	-	-	2,565	1,425	1,710	5,700	2,565	1,425	1,710	5,700
<b>Total pilot compensation</b>	<b>\$ 1,217,659</b>	<b>\$ 676,478</b>	<b>\$ 811,773</b>	<b>\$ 2,705,910</b>	<b>\$ (115,913)</b>	<b>\$ (64,396)</b>	<b>\$ (77,275)</b>	<b>\$ (257,584)</b>	<b>\$ 1,101,746</b>	<b>\$ 612,082</b>	<b>\$ 734,498</b>	<b>\$ 2,448,326</b>
<b>Operating expenses</b>												
<b>Other pilotage costs</b>												
Pilot subsistence/Travel (D3-13-03)	\$ 202,787	\$ 112,660	\$ 135,191	\$ 450,638	\$ (3,110)	\$ (1,728)	\$ (2,073)	\$ (6,910)	\$ 199,677	\$ 110,932	\$ 133,118	\$ 443,728
License insurance	8,309	4,616	5,540	18,465	-	-	-	-	8,309	4,616	5,540	18,465
Payroll taxes (D3-13-01)	-	-	-	-	62,318	34,621	41,546	138,485	62,318	34,621	41,546	138,485
Other	9,398	5,221	6,266	20,885	-	-	-	-	9,398	5,221	6,266	20,885
<b>Total other pilotage costs</b>	<b>220,494</b>	<b>122,497</b>	<b>146,997</b>	<b>489,988</b>	<b>59,208</b>	<b>32,893</b>	<b>39,473</b>	<b>131,575</b>	<b>279,702</b>	<b>155,390</b>	<b>186,470</b>	<b>621,563</b>
<b>Pilot boat and dispatch costs</b>												
Pilot boat costs	261,212	145,118	174,141	580,471	-	-	-	-	261,212	145,118	174,141	580,471
Dispatch costs	84,264	46,814	56,176	187,254	-	-	-	-	84,264	46,814	56,176	187,254
Payroll taxes	9,408	5,227	6,272	20,907	-	-	-	-	9,408	5,227	6,272	20,907
<b>Total pilot boat and dispatch costs</b>	<b>354,884</b>	<b>197,159</b>	<b>236,589</b>	<b>788,632</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>354,884</b>	<b>197,159</b>	<b>236,589</b>	<b>788,632</b>
<b>Administrative expenses</b>												
Legal - general counsel	340	189	227	756	-	-	-	-	340	189	227	756
Legal - shared counsel (K&L Gates)	12,156	6,754	8,104	27,014	-	-	-	-	12,156	6,754	8,104	27,014
Office rent	4,455	2,475	2,970	9,900	-	-	-	-	4,455	2,475	2,970	9,900
Insurance	4,859	2,699	3,239	10,797	-	-	-	-	4,859	2,699	3,239	10,797
Employee benefits	73,801	41,001	49,201	164,003	-	-	-	-	73,801	41,001	49,201	164,003
Payroll taxes	6,163	3,424	4,109	13,696	-	-	-	-	6,163	3,424	4,109	13,696
Other taxes	830	461	553	1,844	-	-	-	-	830	461	553	1,844
Depreciation/Auto leasing/Other	14,542	8,079	9,695	32,316	-	-	-	-	14,542	8,079	9,695	32,316
Interest	1,442	801	961	3,204	-	-	-	-	1,442	801	961	3,204
APA Dues	11,337	6,299	7,558	25,194	-	-	-	-	11,337	6,299	7,558	25,194
Dues and subscriptions (D3-13-02)	2,565	1,425	1,710	5,700	(2,565)	(1,425)	(1,710)	(5,700)	-	-	-	-
Utilities	19,603	10,891	13,069	43,563	-	-	-	-	19,603	10,891	13,069	43,563
Salaries	53,515	29,731	35,677	118,923	-	-	-	-	53,515	29,731	35,677	118,923
Accounting/Professional fees	12,409	6,894	8,273	27,576	-	-	-	-	12,409	6,894	8,273	27,576
Pilot training	-	-	-	-	-	-	-	-	-	-	-	-
Other taxes	6,755	3,753	4,504	15,012	-	-	-	-	6,755	3,753	4,504	15,012
<b>Total administrative expenses</b>	<b>224,772</b>	<b>124,876</b>	<b>149,850</b>	<b>499,498</b>	<b>(2,565)</b>	<b>(1,425)</b>	<b>(1,710)</b>	<b>(5,700)</b>	<b>222,207</b>	<b>123,451</b>	<b>148,140</b>	<b>493,798</b>
<b>Total operating expenses</b>	<b>\$ 800,150</b>	<b>\$ 444,532</b>	<b>\$ 533,436</b>	<b>\$ 1,778,118</b>	<b>\$ 56,643</b>	<b>\$ 31,468</b>	<b>\$ 37,763</b>	<b>\$ 125,875</b>	<b>\$ 856,793</b>	<b>\$ 476,000</b>	<b>\$ 571,199</b>	<b>\$ 1,903,993</b>
<b>Total pilot compensation and operating expenses</b>	<b>\$ 2,017,809</b>	<b>\$ 1,121,010</b>	<b>\$ 1,345,209</b>	<b>\$ 4,484,028</b>	<b>\$ (59,270)</b>	<b>\$ (32,928)</b>	<b>\$ (39,512)</b>	<b>\$ (131,709)</b>	<b>\$ 1,958,539</b>	<b>\$ 1,088,082</b>	<b>\$ 1,305,697</b>	<b>\$ 4,352,319</b>

\* Includes \$1,121,030 of 2013 distributions that were not subject to the agreed-upon procedures in Section II

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

#### III. VARIANCE ANALYSIS

##### Procedure:

Obtain a listing of the expenses incurred by District 3 for the years ended December 31, 2009, through December 31, 2013, and perform the following procedures:

1. Segregate accounts into groups based on account description.
2. Compute average of the accounts and groups from 2009 to 2013.
3. Compute difference between the actual balance for each year and the average for each account and group.
4. Compute percentage difference between the actual balance for each year and the average for each account and group.
5. Using the results of procedure number 3 above, identify differences that are greater than 1/3 of PeM. Using the results of procedure number 4 above, identify differences that are greater than 10%. Review remaining account and group analytics and judgmentally determine if any should be selected for additional review.
6. Review the account and group analysis and perform the following procedures:
  - A. Compute pilot compensation as a percentage of revenue;
  - B. Compute pilot boat expense as a percentage of revenue;
  - C. Compute health insurance per pilot;
  - D. Compute travel expense per pilot; and
  - E. Compute training expense per pilot.
7. Obtain explanation and supporting documentation from pilot association personnel, if deemed necessary, to support identified variances and determine if reasonable.
8. Determine whether any instances were identified that led us to believe 2013 expenses were overstated for ratemaking purposes.

##### Results:

No exceptions were noted as a result of performing such procedures.

**Western Great Lakes Pilots Association, LLP**

**Summary of Agreed-Upon Procedures and Results**

**IV. INVESTMENT BASE CALCULATION**

Procedure:

Prepare the Investment Base Calculation using information obtained from the audited financial statements of Western Great Lakes Pilots Association, LLP for the year ended December 31, 2013:

	Area 6	Area 7	Area 8	District 3
<b>Recognized assets</b>				
Total current assets	\$ 723,394	\$ 401,886	\$ 482,263	\$ 1,607,543
Total current liabilities	112,784	62,658	75,190	250,632
Current notes payable	9,335	5,186	6,224	20,745
Total property and equipment (NET)	22,199	12,333	14,799	49,330
Land	-	-	-	-
Total other assets	450	250	300	1,000
<b>Total recognized assets</b>	<b>642,594</b>	<b>356,997</b>	<b>428,396</b>	<b>1,427,986</b>
<b>Non-recognized assets</b>				
Total investments and special funds	-	-	-	-
<b>Total non-recognized assets</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total assets</b>				
Total recognized assets	642,594	356,997	428,396	1,427,986
Total non-recognized assets	-	-	-	-
<b>Total assets</b>	<b>\$ 642,594</b>	<b>\$ 356,997</b>	<b>\$ 428,396</b>	<b>\$ 1,427,986</b>
<b>Recognized sources of funds</b>				
Total stockholders' equity	\$ 627,232	\$ 348,462	\$ 418,155	\$ 1,393,849
Long-term debt	6,026	3,348	4,018	13,392
Current notes payable	9,336	5,187	6,223	20,745
Advances from affiliated companies	-	-	-	-
Long-term obligations - capital leases	-	-	-	-
<b>Total recognized sources</b>	<b>642,594</b>	<b>356,997</b>	<b>428,396</b>	<b>1,427,986</b>
<b>Non-recognized sources of funds</b>				
Pension liability	-	-	-	-
Other non-current liabilities	-	-	-	-
Deferred federal income taxes	-	-	-	-
Other deferred credits	-	-	-	-
<b>Total non-recognized sources</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total sources of funds</b>				
Total recognized sources	642,594	356,997	428,396	1,427,986
Total non-recognized sources	-	-	-	-
<b>Total sources of funds</b>	<b>\$ 642,594</b>	<b>\$ 356,997</b>	<b>\$ 428,396</b>	<b>\$ 1,427,986</b>

Results:

No exceptions were noted as a result of performing such procedures.

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

#### V. COMPARISON OF PILOT ASSOCIATION ACTIVITIES

##### Procedure:

Obtain a listing of the expenses incurred by St. Lawrence Seaway Pilots' Association and Seaway Pilot Inc. (collectively known as District 1), Lakes Pilots Association, Inc. (District 2) and District 3 for the year ended December 31, 2013 and perform the following procedures:

1. Segregate accounts for each District into four categories: a) Pilotage Compensation (which includes pilot distributions and dividends), b) Other Pilotage Costs, c) Pilot Boat and Dispatch Costs, and d) Administrative Expenses.
2. For each District, compare 2013 expenses and the percentage of each expense, to total district revenue.
3. Perform an analysis of the significant cost categories incurred by the Districts and provide a summary of the composition of the following categories:
  - A. Pilot compensation and payroll taxes,
  - B. Pilot subsistence/travel,
  - C. Pilot boat and dispatch costs,
  - D. Cost associated with affiliated entities, and
  - E. Administrative expenses,
    - i. Legal, accounting and professional fees,
    - ii. Office rent, and
    - iii. Depreciation/auto leasing/other.

**Western Great Lakes Pilots Association, LLP**  
**Summary of Agreed-Upon Procedures and Results**

**Results:**

The following are the results of performing such procedures for the year ended December 31, 2013:

	District 1		District 2		District 3		Total	
	<u>\$</u>		<u>\$</u>		<u>\$</u>		<u>\$</u>	
	Adjusted amount	% of district revenue						
Total revenue	<u>3,694,379</u>		<u>3,607,407</u>		<u>4,551,550</u>		<u>11,853,336</u>	
Pilot compensation								
Salaries	\$ 2,171,804	58.79%	\$ 1,576,940	43.71%	\$ 1,964,539	43.16%	\$ 5,713,283	48.20%
Applicant pilot salaries	67,818	1.84%	57,991	1.61%	60,000	1.32%	185,809	1.57%
Employee benefits	107,555	2.91%	475,157	13.17%	396,065	8.70%	978,777	8.26%
Applicant pilot employee benefits	-	0.00%	17,882	0.50%	22,022	0.48%	39,904	0.34%
Dues and Subscriptions	4,200	0.11%	2,785	0.08%	5,700	0.13%	12,685	0.11%
Total pilot compensation	<u>\$ 2,351,377</u>	<u>63.65%</u>	<u>\$ 2,130,755</u>	<u>59.07%</u>	<u>\$ 2,448,326</u>	<u>53.79%</u>	<u>\$ 6,930,458</u>	<u>58.47%</u>
Operating expenses								
Other pilotage costs								
Pilot subsistence/Travel	\$ 449,996	12.18%	\$ 210,410	5.83%	\$ 443,728	9.75%	\$ 1,104,134	9.31%
License insurance	51,986	1.41%	15,420	0.43%	18,465	0.41%	85,871	0.72%
Payroll taxes	113,465	3.07%	112,328	3.11%	138,485	3.04%	364,278	3.07%
Other	12,385	0.34%	82,553	2.29%	20,885	0.46%	115,823	0.98%
Total other pilotage costs	<u>627,832</u>	<u>16.97%</u>	<u>420,711</u>	<u>11.65%</u>	<u>621,563</u>	<u>13.65%</u>	<u>1,670,106</u>	<u>14.08%</u>
Pilot boat and dispatching costs								
Pilot boat costs	233,270	6.31%	357,341	9.91%	580,471	12.75%	1,171,082	9.88%
Dispatching costs	-	0.00%	17,700	0.49%	187,254	4.11%	204,954	1.73%
Employee benefits	-	0.00%	151,662	4.20%	-	0.00%	151,662	1.28%
Payroll taxes	16,399	0.44%	20,790	0.58%	20,907	0.46%	58,096	0.49%
Total pilot boat and dispatch costs	<u>249,669</u>	<u>6.76%</u>	<u>547,493</u>	<u>15.17%</u>	<u>788,632</u>	<u>17.33%</u>	<u>1,585,794</u>	<u>13.38%</u>

**Western Great Lakes Pilots Association, LLP**  
**Summary of Agreed-Upon Procedures and Results**

	District 1		District 2		District 3		Total	
Total revenue	<u>\$ 3,694,379</u>		<u>\$ 3,607,407</u>		<u>\$ 4,551,550</u>		<u>\$ 11,853,336</u>	
	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue	Adjusted amount	% of district revenue
Administrative expenses								
Legal - general counsel	1,129	0.03%	8,536	0.24%	756	0.02%	10,421	0.09%
Legal - shared counsel (K&L Gates)	22,776	0.62%	18,260	0.51%	27,014	0.59%	68,050	0.57%
Legal - USCG litigation	-	0.00%	577	0.02%	-	0.00%	577	0.00%
Office rent	-	0.00%	65,688	1.82%	9,900	0.22%	75,588	0.64%
Insurance	40,281	1.09%	17,031	0.47%	10,797	0.24%	68,109	0.57%
Employee benefits	18,931	0.51%	50,564	1.40%	164,003	3.60%	233,498	1.97%
Payroll taxes	9,282	0.25%	12,248	0.34%	13,696	0.30%	35,226	0.30%
Other taxes	39,661	1.07%	37,029	1.03%	1,844	0.04%	78,534	0.66%
Travel	937	0.03%	-	0.00%	-	0.00%	937	0.01%
Depreciation/Auto leasing/Other	75,618	2.05%	41,412	1.15%	32,316	0.71%	149,346	1.26%
Interest	27,094	0.73%	8,598	0.24%	3,204	0.07%	38,896	0.33%
APA Dues	24,510	0.66%	20,520	0.57%	25,194	0.55%	70,224	0.59%
Dues and subscriptions	500	0.01%	-	0.00%	-	0.00%	500	0.00%
Utilities	8,798	0.24%	35,775	0.99%	43,563	0.96%	88,136	0.74%
Salaries	96,844	2.62%	106,582	2.95%	118,923	2.61%	322,349	2.72%
Accounting/Professional fees	9,100	0.25%	23,234	0.64%	27,576	0.61%	59,910	0.51%
Pilot training	-	0.00%	-	0.00%	-	0.00%	-	0.00%
Other	15,789	0.43%	24,395	0.68%	15,012	0.33%	55,196	0.47%
Total administrative expenses	<u>391,250</u>	<u>10.60%</u>	<u>470,449</u>	<u>13.03%</u>	<u>493,798</u>	<u>10.85%</u>	<u>1,355,497</u>	<u>11.44%</u>
Total operating expenses	<u>\$ 1,268,751</u>	<u>34.34%</u>	<u>\$ 1,438,653</u>	<u>39.87%</u>	<u>\$ 1,903,993</u>	<u>41.83%</u>	<u>\$ 4,611,397</u>	<u>38.90%</u>
Total pilot compensation and operating expenses	<u>\$ 3,620,128</u>	<u>97.99%</u>	<u>\$ 3,569,408</u>	<u>98.95%</u>	<u>\$ 4,352,319</u>	<u>95.62%</u>	<u>\$ 11,541,855</u>	<u>97.37%</u>

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

#### Pilot Compensation and Payroll Taxes

- District 1: Pilots were compensated through capital draws based on available funds. Therefore, pilot salary expenses are not recorded in the audited financial statements. All capital drawings have been allocated to pilot compensation or other expenses as deemed appropriate. The pilots were responsible for paying payroll taxes within their personal tax filing. The district did not record a 'self-employment tax equivalent' in the Statement of Pilots' Capital, in its audited financial statements for the year ended December 31, 2013; however, a pilot payroll tax expense was reported by the district. This amount was computed by multiplying total pilot advances by the IRS standard self-employment tax rate of 15.3%, consisting of 12.4% for social security and 2.9% for Medicare, up to \$113,700. Compensation in excess of \$113,700 is subject to the 2.9% Medicare tax only. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.
- District 2: Pilots were compensated on a 'per available day' basis at either \$200 or \$150 per day. Pilots also received other special compensation payments as determined during the year. Payroll taxes were computed and recorded by the association based on IRS guidelines.
- District 3: Pilots were compensated on a 'per available day' basis at an agreed-upon daily rate. The pilots also receive distributions, which are included in pilot compensation for the purposes of this report. The pilots were responsible for paying payroll taxes within their personal tax filing. Therefore, payroll taxes on pilot compensation were not recorded by the Association. An adjustment was made to reclassify the expected employer portion of the payroll taxes, using IRS standard tax rates of 6.2% for Social Security and 1.45% for Medicare.

#### Pilot Subsistence/Travel

- District 1: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.
- District 2: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately 200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.
- District 3: All travel expenses incurred, such as hotel or taxi charges, were generally reimbursed at actual costs and require a receipt to be submitted. Per diem reimbursements were calculated at a rate of \$59 per day based on approximately

## **Western Great Lakes Pilots Association, LLP**

### **Summary of Agreed-Upon Procedures and Results**

200 days per year which is considered the length of time of the normal operating season of the pilots starting in April and ending in December.

#### Pilot Boat and Dispatch Costs

- District 1: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. District 1 did not incur dispatch charges, as dispatching was provided by the Canadian Great Lakes Pilotage Authority in exchange for pilot boat services.
- District 2: This District owns pilot boats and incurred costs to operate these boats, such as salaries, fuel and maintenance. This District provided pilot boat services to its own pilots, as well as pilots from District 3 and Canada. Total expenses incurred were reduced by the revenue incurred from these services. This District also incurred dispatch expenses.
- District 3: This District received pilot boat services from several entities at its various ports, including District 2. This District employed dispatchers to handle its dispatch needs.

#### Costs Associated with Affiliated Entities

- District 1: Seaway Pilot Inc. is an affiliate of St. Lawrence Seaway Pilots' Association and provides services such as pilot boat operations, bookkeeping and administration services, and equipment rental. Expenses incurred by St. Lawrence Seaway Pilots' Association related to these services were eliminated for these agreed-upon procedures.
- District 2: This District leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually. In addition to the required monthly lease payments, the lease agreement requires payments of utilities, maintenance and property taxes.
- District 3: This District did not enter into transactions with or make payments to affiliated entities.

#### Administrative Expense

##### Legal, Accounting and Professional Fees:

- District 1: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.
- District 2: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. During 2013, the District incurred legal expenses related to ongoing litigation with the United States Coast Guard. The

## Western Great Lakes Pilots Association, LLP

### Summary of Agreed-Upon Procedures and Results

District also incurred accounting fees for preparation of audited financial statements and tax returns.

District 3: This District incurred legal expenses for its operations and in conjunction with the other districts, with a shared attorney used for common issues affecting the pilot associations and the ratemaking process. The District also incurred accounting fees for preparation of audited financial statements and tax returns.

#### Office Rent:

District 1: This District did not incur office rent expense. It operated in a building owned by Seaway Pilot Inc.

District 2: This district leased property from an affiliated entity at a monthly rate of \$5,474, or \$65,688 annually.

District 3: This District leased office space from an unrelated party on a month-to-month basis at an amount equal to \$9,900 annually.

#### Depreciation/Auto Leasing/Other:

District 1: This District incurred depreciation on an office building, pilot boats and various pieces of equipment.

District 2: This District incurred depreciation on pilot boats, a housing location at one port, and various pieces of equipment. The District also entered into automobile lease agreements.

District 3: This District incurred depreciation on equipment and vehicles.

## VI. RECOMMENDED GENERAL LEDGER ACCOUNTS

#### Procedure:

Recommend a list of general ledger accounts for use by each Association.

#### Results:

As a result of performing the aforementioned agreed-upon procedures, we recommend the Districts incorporate the account groupings listed in Procedures I and III into the financial data provided to the Great Lakes Pilotage Division for analysis, understanding that more detailed subaccounts would be necessary to accurately classify expenses incurred.

**Western Great Lakes Pilots Association, LLP**

**Summary of Findings and Recommendations**

The following findings detail adjustments necessary for ratemaking purposes, as identified in section II of the previous report.

Finding Number: D3-13-01

Finding Title: Pilot Salaries and Payroll Taxes

Condition:

The Association improperly recorded payroll taxes for pilot compensation as the pilots are responsible for these on their individual tax returns.

Criteria:

Federal Register, Vol. 70, No. 46, section 12091 dated March 10, 2005 allows for estimated Social Security and Medicare taxes to be recorded on behalf of the Association when these taxes are incurred by the pilots on their individual tax returns.

Effect:

Operating expenses are understated and pilot compensation is overstated.

Cause:

The pilots of the Association are self-employed, therefore they incur these payroll costs on their individual tax returns.

Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

Finding Number: D3-13-02

Finding Title: Dues and Subscriptions

Condition:

The Association incurred costs for dues and subscriptions that were classified as operating expenses.

Criteria:

Regulation 46 CFR 404.5(a)(8)(v) states that expenses not directly related to pilotage are not recognized as reasonable for ratemaking purposes.

Effect:

Pilot compensation is understated and expenses are overstated.

## **Western Great Lakes Pilots Association, LLP**

### **Summary of Findings and Recommendations**

#### Cause:

The classifications of expenses in the Association's audited financial statements and trial balance are not tailored for ratemaking submission purposes.

#### Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.

#### Finding Number: D3-13-03

Finding Title: Pilot Subsistence/Travel

#### Condition:

The Association recorded and paid for cost in 2013 that were incurred in 2012 and did not have appropriate documentation to support some costs.

#### Criteria:

The scope of this report is that only 2013 expenses are allowable for ratemaking purposes. Regulation 46 CFR 404.5(a)(8)(i) states that undocumented expenses are not recognized as reasonable for ratemaking purposes.

#### Effect:

Operating expenses are overstated.

#### Cause:

Expenses incurred in 2012 were recorded and paid during 2013 and all costs must be documented and demonstrated that they are necessary and reasonable in order to be reimbursable.

#### Recommendation:

Expenses submitted for ratemaking should be in a standard format approved by the U.S. Coast Guard, detailing adjustments necessary to comply with ratemaking standards.